DIRECTOR-GENERAL OF INLAND REVENUE v. T.M. SDN. BHD.

[A.C.J. (Gill F.J.) December 16, 1972]

[Kuala Lumpur — Originating Mortion No. 18 of 1972]

Income Tax — Deduction — Qualifying mining expenditure — Income Tax (Mining Operations) Rules, 1949 — Income Tax Act, 1967, s. 34(6), Schedules 2 & 9.

In this case the T.M. Sdn. Bhd. had bought a tin mine for the sum of $2.5 million. They also incurred capital expenditure on the development of the mine. They claimed that the sum of $2.5 million which they had paid as the purchase price of the mine should have been treated as qualifying mining expenditure and that the amount of $1,421,261.75 which they claimed they spent in the development of the mine should also be so treated. The Special Commissioners held that the sum of $2.5 million should be treated as qualifying mining expenditure but they rejected the claim in respect of the other sum as there was no satisfactory evidence to show that the expenditure was qualifying mining expenditure. The appellant appealed against this decision by way of case stated.

Held: the sum of $2.5 million was rightly held to be qualifying mining expenditure as the respondents had became the owner of the land and the expenditure was incurred for the acquisition of the mine which was the site of the source of the mineral deposits. Applying the formula laid down in paragraph 3 of Schedule 2 to the Income Tax Act, the total qualifying expenditure incurred by the respondents should be apportioned for the four years estimated life of the mine at the time of the purchase.

Case referred to:-

(1) *Bachan Singh* v. *Mohinder Kaur* [1956] M.L.J. 97.

CASE STATED.

Nik Saghir bin Mohamad Noor (Senior Federal Counsel) for the appellant.

J. Puthucheary for the respondents.

Gill F.J.: This is an appeal by way of case stated by the Special Commissioners of Income Tax under paragraph 34 of Schedule 5 to the Income Tax Act, 1967 on the requisition of the Director-General of Inland Revenue, the appellant.

The facts of the case as found by the Special Commissioners are as follows. The Eastern Mining and Metals Co. Ltd. (hereinafter referred to as EMMCO), having been incorporated on August 5, 1948, bought from the Custodian of Enemy Property in that year 1,180.1 acres of mining land in the District of Dungun in the State of Trengganu for a sum of 2 million dollars. Mining operations on the land for iron ore were commenced in 1953 but production of the ore did not begin until about the beginning of June, 1956. Not much mining activity took place on two areas of the land known as Sri Bangun and Batu Tiga, because of the low iron content which was contaminated by sulphur and tin.

T. M. Sendirian Berhad, the respondent company, was incorporated on March 12, 1956 as an associate of EMMCO with a common directorship. On October 15, 1964 EMMCO granted a sublease to the respondents for the mining of tin ore at Sri Bangun and Batu Tiga, the latter locality being 218 acres in area. On December 31, 1966 the two companies entered into an agreement whereby EMMCO sold to the respondents the Batu Tiga mine with effect from January 1, 1967 for a sum of $2.5 million, the Sri Bangun area being not included in the sale. Resolutions confirming the purchase and sale of the Batu Tiga mine were passed by the respondents and EMMCO on January 30, 1967 and October 23, 1968 respectively.

The sale agreement provided, *inter alia*, that EMMCO would use their best endeavours to obtain separate and transferable titles in respect of the Batu Tiga mine and would, when this was achieved, execute and deliver to the respondents registrable transfers in respect of the said mine upon the respondents in turn executing a surrender of the sub-lease which had been granted to them by EMMCO. Pending the execution and registration of such documents of transfer, the respondents were permitted under clause 4 of the agreement, as purchasers in possession, to occupy, enjoy and work the mine as from January 1, 1967.

The original cost of the Batu Tiga area to EMMCO was unknown, as it was purchased together with the rest of their lands in Dungun for a lump sum, nor was the expenditure incurred in the development of Batu Tiga mine available. In the ledger of EMMCO for the years 1955-1956 the value of all their lands in the District of Dungun, including the Batu Tiga area, was shown as $133,149.40 as on January 1, 1955. Messrs. Valentine & Dunne, a firm of mining consultants, however, valued the said lands, on the Hoskold Present Value formula for the valuation of mining land, at a little over 25 million dollars as at the end of 1955.

It is to be observed that the price paid by the respondents to EMMCO for the Batu Tiga mine was 10 per cent of the amount at which Messrs. Valentine & Dunne had valued the entire area of EMMCO's lands in the District of Dungun as at the end of 1955. On that basis, the appellant fixed the original cost of Batu Tiga mine at 10 per cent of $133,149.40 which was the value of the lands as shown in EMMCO's ledger as on January 1, 1955. For the sake of convenience, however, he rounded up the cost to $20,000. In respect of the additional assessments of income tax of the respondents for the years of assessment 1968, 1969 and 1970, he therefore allowed that sum of $20,000 as the qualifying mining expenditure under section 34(6)(c) and paragraph 13(1) of Schedule 2 of the Income Tax Act, 1967.

From 1951 to 1962, EMMCO had claimed and were allowed depletion allowances on capital expenditure incurred by them on their land in Dungun to the extent of $7,382,101. For the years of assessment 1965 and 1966, the respondents had claimed and were allowed depletion allowances in respect of capital expenditure on Batu Tiga mine when they were sublessees and not owners of the mine. This capital expenditure was incurred in drilling and surveying the Batu Tiga area.

On appeal to the Special Commissioners, the respondents claimed that the sum of $2.5 million which they paid as the purchase price for Batu Tiga mine, and not merely $20,000, should have been treated as qualifying mining expenditure. They also sought to prove that before the Batu Tiga mine was sub-leased and subsequently sold to them, EMMCO had incurred direct capital expenditure amounting to $1,421,261.75

on the development of the mine. They, therefore, claimed that that amount should also be treated as qualifying mining expenditure.

On the evidence before them, the Special Commissioners reached the conclusion that as, by virtue of the sale agreement, the respondents became the owners of Batu Tiga mine on January 1, 1967, their case was governed by paragraph 41 of Schedule 9 to the Income Tax Act, 1967. They, therefore, went on to hold that the respondents owned a mining asset as defined in paragraph 6 of Schedule 2 at the beginning of the basis period for the year of assessment 1968, that they had incurred a sum of $2.5 million as capital expenditure as defined in the Income Tax (Mining Operations) Rules, 1949 on or for the asset and that such capital expenditure should be treated as qualifying mining expenditure. Under the circumstances, they made a deciding order that the additional assessments of income tax of the respondents for the years of assessment 1968, 1969 and 1970 be amended accordingly.

The claim in respect of the direct capital expenditure of $1,421,261.75 which EMMCO had allegedly incurred for the development of the Batu Tiga mine, however, was rejected on the ground that there was no satisfactory evidence to show that the expenditure was qualifying mining expenditure as specified in Schedule 2, or that it was capital expenditure within the meaning of the Income Tax (Mining Operations) Rules, 1949.

There being no appeal by the respondents against the rejection of their alternative claim, the sole question for determination in this appeal is whether the respondent company is entitled to have the sum of $2.5 million deducted from their gross income for the purpose of ascertaining their adjusted income, as decided by the Special Commissioners.

The general principle with regard to deduction of expenses for the purpose of ascertaining the adjusted income of a person is that expenses which are of revenue nature, that is, expenses incurred in the production of income, are deductible. On the other hand, capital expenditure is generally not deductible. However, tax payers engaged in mining operations are given certain concessions in that certain items of expenditure, though capital in nature, are expressly allowed as deductions under the Income Tax Act, 1967. Thus section 34(6)(c) of the Act provides:

"There may be deducted from the relevant gross income — where any part of the relevant gross income is derived from the working of a mine, such amounts in respect of capital expenditure as may be allowed for the relevant period pursuant to Schedule 2."

These deductions in respect of capital expenditure on mines are known as "qualifying mining expenditure", which is defined in paragraph 1 of Schedule 2 as follows:

"Subject to paragraph 2, qualifying mining expenditure for the purposes of this Schedule is expenditure which is incurred in connection with the working of a mine or in preparation for the working of a mine —

(a) on the acquisition of the mine or rights in or over the mine;

(b) on searching for, on discovering and testing or on winning access to deposits of minerals;

(c) on the construction of any works or buildings which, when the mine ceases to be worked, are likely to be of little or no value to any person except in connection with the working of another mine; or

(d) on development, general administration or management before the production of minerals begins or during any period when minerals are not being produced."

It is to be observed that paragraph 1 of Schedule 2 merely defines "qualifying mining expenditure" but does not quantify the amount of expenditure to be deducted from the gross income. A provision for that is made in paragraph 3 of Schedule 2, which reads:

"Subject to this Schedule, where the business of a person consists or mainly consists of the working of a mine with or without other mines (that business and that person being in this Schedule referred to as the relevant business and the operator respectively) and the operator has incurred qualifying mining expenditure in relation to that mine, then, in the ascertainment of the adjusted income of the operator for the basis period for a year of assessment from the relevant business there shall be allowed pursuant to this Schedule as a deduction under section 34 from the gross income for that period from the relevant business an amount arrived at by dividing the residual expenditure at the end of that period by the residual life at the beginning of that period."

"Residual expenditure" and "residual life" are defined in paragraph 22 of the same Schedule as follows: —

"residual expenditure", in relation to any particular mine forming part of the relevant business and to any particular date, means the total qualifying mining expenditure incurred in respect of that mine before the date by the operator, reduced by the amount of —

(a) any deduction made under section 34 pursuant to this Schedule in respect of that expenditure from the gross income of the operator from the relevant business for the basis period for any year of assessment, being a basis period ending before that date; and

(b) any recovered expenditure in relation to that mine received by the operator on or before that date;

"residual life", in relation to any particular mine forming part of the relevant business and to any particular date, means the number of years of the estimated life of the mine remaining at that date.

As I have already said, the appellant allowed the respondents a sum of $20,000 as qualifying mining expenditure. He did this under paragraph 13(1) of Schedule 2, which says:

"Where the operator has incurred expenditure in relation to the transfer to him of the mine and any other matter or thing appertaining to the mine. that expenditure or the total qualifying mining expenditure incurred by the transferor in respect of the mine, whichever is the less, shall be treated as qualifying mining expenditure incurred by the operator in respect of the mine".

The Special Commissioners, however, held paragraph 13(1) of Schedule 2 to be irrelevant and inapplicable to the facts of the present case, which in their opinion was governed by paragraph 41 of Schedule 9 to the Act. Paragraph 41 of Schedule 9 provides:

"For the purposes of Schedule 2, where the operator owned an asset at the beginning of the basis period for the year of assessment 1968 and has incurred capital expenditure as defined in the Income Tax (Mining Operations) Rules, 1949, of West Malaysia on or for the asset in connection with the working of the mine —

(a) the asset shall be deemed to be included in the definition of 'mining asset' in paragraph 6 of that Schedule; and

(b) that capital expenditure shall be treated as qualifying mining expenditure."

Capital expenditure is defined by rule 2(ii) of the Income Tax (Mining Operations) Rules, 1949 as follows: —

" 'capital expenditure' means expenditure in connection with the carrying on of mining operations incurred:

(a) on the acquisition of the site of the source of mineral deposits, or the site of any works as defined under sub-paragraph (c), or of rights in or over any such site or rights in or over the deposits; or

(b) on searching for or on discovering and testing deposits, or winning access thereto; or

(c) on the construction of any works which are likely to be of little or no value when the source is no longer worked; or

(d) on development, general administration and management prior to commencement of production or during any period of non-production:

Provided that the expression does not include —

expenditure in respect of which a deduction is allowed under any other provision of the Ordinance and in particular does not include expenditure on plant and machinery, and extra-ordinary expenditure within the meaning of section 22c of the Ordinance."

"Mining asset", as defined in paragraph 6 of Schedule 2, "means either the mine or an asset on or for which the operator has incurred qualifying mining expenditure in connection with or in preparation for the working of the mine".

The major ground of appeal on behalf of the appellant is that the Special Commissioners misconstrued the scope and effect of paragraph 41 of Schedule 9. It is said that paragraph 41 is a transitional and saving provision, its function being to bridge the gap between the repealed 1947 Income Tax Ordinance and the 1967 Income Tax Act as well as to save certain rights to deduction of capital expenditure. This, it is explained, is necessary because capital expenditure in connection with the working of a mine is not allowed as a deduction wholly in the year in which it is incurred but is spread over a number of years depending on the estimated life of the mine. For instance, if capital expenditure which qualifies for deduction was incurred in 1955 and the estimated life of the mine was 10 years, then the deduction to be given in respect of that expenditure is spread over to 1965 in accordance with certain formula laid down by the Income Tax (Mining Operations) Rules, 1949. If, on the other hand, the expenditure was incurred in 1965 and the estimated life of the mine was also 10 years, the spreading of the deduction would have gone into the years covered by the Income Tax Act, 1967 which came into force commencing from year of assessment 1968. The deduction (commonly known as depletion allowance) to which the operator would have been entitled under the repealed 1947 Ordinance would not then be available to him in 1968 but for the transitional and saving provisions contained in paragraph 41 of Schedule 9. In other words, without paragraph 41, the operator will not in 1968 and thereafter be able to claim as a deduction the balance of the allowance on capital expenditure still due to him under the repealed 1947 Ordinance. With that exposition of the object of paragraph 41 of Schedule 9 by counsel for the appellant, Encik Nik Saghir, I entirely agree.

It is next said that paragraph 41 is also a deeming provision in that it deems two things. First, it deems the Batu Tiga mine to be included in the definition of "mining asset" for the purpose of Schedule 2. Secondly, it deems the capital expenditure incurred on the asset to be the qualifying mining expenditure. It is argued that for the deeming provision to operate, two conditions must be satisfied. First, the operator must own an asset at the beginning of the basis period for the year of assessment 1968. Secondly, the operator must have incurred capital expenditure as defined in the Income Tax (Mining Operations) Rules, 1949 on or for the asset in connection with the working of the mine.

It is then submitted that the second condition has not been satisfied for two reasons. The first of these reasons, based on the authority of *Bachan Singh* v. *Mahinder Kaur*,[1] is that the sum of $2.5 million was paid by the respondents not for the acquisition of the site of the source of mineral deposits or for the acquisition of rights in or over the deposits, but for the acquisition of right *ad rem* and *in personam* which is in the nature of a chose in action. I do not think I can accept that submission. The respondents had paid the money for the purchase of the Batu Tiga mine. They were put in possession and were allowed to operate the mine as from January 1, 1967. It is true that the land in question had not been transferred to them, but that was because separate titles had to be obtained for the land sold before any registrable transfers could be executed. Under those circumstances, they became owners in all respects except in name. In other words, they became the equitable owners of the land comprised in Batu Tiga mine.

The second reason given for the second condition not having been satisfied is that, even assuming that the $2.5 million is the cost of Batu Tiga mine and therefore capital expenditure within the meaning of rule 2(ii)(a) of the Income Tax (Mining Operations) Rules, 1949, such expenditure was not expenditure incurred *on or for the asset in connection with the working of the mine* as stipulated in paragraph 41 of Schedule 9. With all respect to the learned counsel for the appellant, this argument is a mere quibble. The money was clearly paid for the acquisition of the mine which was the site of the source of the mineral deposits. The mine being the site of the source of mineral deposits, it was an asset on or for which the respondents had incurred the capital expenditure of $2.5 million. How then can it be said that paragraph 41 of Schedule 9 does not apply to the facts of this case?

The second ground of appeal is that even if the Special Commissioners have correctly decided that paragraph 41 of Schedule 9 applies to the present case, they have erred in law in saying that paragraph 13(1) of Schedule 2 is irrelevant. It is said that in so doing they have ignored the intention of the legislature in enacting paragraph 41 of Schedule 9. It is argued that paragraph 41 is not intended to preclude the operation of paragraph 13 of Schedule 2 in a proper case, especially when in sub-paragraph (a) of paragraph 41 itself there is reference made to paragraph 6 of Schedule 2, which says that "paragraphs 7 to 14 shall apply in relation to any particular mine forming part of the relevant business with respect to which the opera-

tor has incurred qualifying expenditure". The weakness of this argument lies in the fact that sub-paragraph (a) of paragraph 41 of Schedule 9 speaks merely of the definition of "mining asset" in paragraph 6 of Schedule 2 and does not refer to the rest of the provision of that paragraph.

It was contended on behalf of the respondents before the Special Commissioners that paragraph 13(1) of Schedule 2 is not applicable as there was no transfer of the mine in accordance with the provisions of section 215 of the National Land Code. The respondents construed the words 'transfer of the mine' appearing in paragraph 13 to mean a transfer which has been registered under the relevant provisions of the National Land Code. That contention, however, was rejected by the Special Commissioners on the ground that on the facts of the present case and considering the tax legislation involved, there was a transfer within the meaning of paragraph 13(1). Their reason for holding that paragraph 13(1) of Schedule 2 was irrelevant and inapplicable, even though they have not stated it, would appear to be obvious. That reason is that the "total qualifying mining expenditure incurred by the transferor in respect of the mine" as specified in that paragraph was unknown, so that the only evidence they had before them was the evidence of the expenditure incurred by the respondents in relation to the transfer to them of the mine.

The last ground of appeal is that the Special Commissioners, in deciding that the respondents were entitled to deduction in respect of the capital expenditure of $2.5 million, completely overlooked the provisions of paragraph 3 of Schedule 2 which lays down the formula to be applied in ascertaining the amount to be allowed as a deduction. With that ground of appeal I entirely agree. The assessments, which are the subject matter of this appeal were assessments for income tax for the years of assessment 1968, 1969 and 1970. That in itself shows the residual life of Batu Tiga mine to be at least 3 years. In all the circumstances of the case, I would agree with counsel for the appellant that it would be reasonable to take 4 years as the residual life of the mine. Applying the formula laid down in paragraph 3 of Schedule 2, on the basis that the total qualifying mining expenditure incurred by the respondents in respect of Batu Tiga mine was $2.5 million and that the estimated life of the mine on the date of its purchase was 4 years, a sum of $625,000 should be deducted from the gross income of each of the years of assessment for the purpose of ascertaining the adjusted income.

For the reasons I have stated, I would allow this appeal with costs. The deciding order of the Special Commissioners would be set aside and there would be an order that the additional assessments of income tax for the years of assessment 1968, 1968 and 1970 as per the three notices of additional assessments dated 24th March, 1971, be amended so as to allow a sum of $625,000 as qualifying mining expenditure in respect of each of those years.

Appeal allowed.

Solicitors: *Skrine & Co.*

NADIMUTHU v. PUBLIC PROSECUTOR

[A.Cr.J. (Abdul Hamid J.) December 18, 1972]

[Kuala Lumpur — Selangor Criminal Appeal No. 25 of 1972]

Bribery and corruption — Medical certificate — Use of false medical certificate to deceive — When such certificate a "document" — Prevention of Corruption Act, 1961, s. 4(c).

A medical certificate must be construed as coming in the category of receipt, account, etc. and for the purposes of section 4(c) of the Prevention of Corruption Act, 1961, the words "other document" include such medical certificate.

Cases referred to:-

(1) *Public Prosecutor* v. *Kyle-Little* [1971] 1 M.L.J. 125.

(2) *Hashim* v. *Public Prosecutor* [1967] 1 M.L.J. 251.

MAGISTRATE' CRIMINAL APPEAL.

Datuk S. P. Seenivasagam for the appellant.

Yusoff Mohamed Noor (Deputy Public Prosecutor) for the respondent.

Abdul Hamid J.: The appellant was convicted by the Kuala Lumpur magistrate on 14 February 1972 on the following charges —

First charge:

That you between 5.8.68 at Sentul Works, Malayan Railways, Sentul, in the district of Kuala Lumpur, in the State of Selangor, being an agent of a public body, namely, employee of the Malayan Railways did knowingly use with intent to deceive your principal, a document, to wit, sick certificate dated 5.8.68 purported to be from the LUM DISPENSARY, Kuala Lumpur, in respect of which your principal is interested and which contained statements which are false in material particulars, in that, you were examined and found to be unfit for duties for one (1) day by Doctor LUM WENG SONG — M.B.B.S. Hong Kong, and which to your knowledge is intended to mislead your principal, and thereby committed an offence punishable under section 4(c) of the Prevention of Corruption Act No. 42 of 1961.

Second charge:

That you between 7.8.68 and 8.8.68 at Sentul Works, Malayan Railways, Sentul, in the district of Kuala Lumpur, in the State of Selangor, being an agent of a public body, namely, employee of the Malayan Railways, did knowingly use with intent to deceive your principal, a document, to wit, sick certificate dated 7.8.68 purported to be from LUM DISPENSARY, Kuala Lumpur in respect of which your principal is interested and which contained statements which are false in material particulars, in that, you were examined and found to be unfit for duties for one (1) day by Doctor LUM WENG SONG — M.B.B.S. Hong Kong, and which to your knowledge is intended to mislead your principal, and that you have thereby committed an offence punishable under section 4(c) of the Prevention of Corruption Act No. 42 of 1961.

He was fined $25 on each charge. The appellant, an employee of the Malayan Railways, submitted two false medical certificates to obtain leave. On the strength of those certificates, he was paid wages for the two days. Subsequently it was discovered that the certificates were false and, as such, the two days' wages paid were recouped from him for reason that he absented from work without leave.

The appeal is against conviction on the ground that reads as follows —

"The learned president ought to have held that the medical certificate was not a 'document' within the meaning assigned to it under section 4(c) of the Prevention of Corruption Act, 1961."

Datuk S.P. Seenivasgam counsel for the appellant cited two cases in support of his argument — *Public*